IN THE SUPREME COURT OF BRITISH COLUMBIA
IN BANKRUPTCY

Citation: *0409725 B.C. Ltd. (Bankruptcy of),*
2015 BCSC 1221

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Docket: B131552
Estate: 11-1820752
Registry: Vancouver

In the Matter of the Bankruptcy of

0409725 B.C. Ltd.

Before: The Honourable Mr. Justice Grauer

Reasons for Judgment

Counsel for the Claims Administrator:	Geoffrey Dabbs
Counsel for the Respondent Owner “M”:	Jeremy West
Place and Date of Hearing:	Vancouver, B.C. July 10, 2015
Place and Date of Judgment:	Vancouver, B.C. July 16, 2015

[2] This continues the saga of the bankruptcy of 0409725 B.C. Ltd., formerly known as Odenza Homes Ltd. These Reasons should be read in conjunction with my earlier Reasons, issued on June 30, 2014 (indexed at 2014 BCSC 1196; the "first Reasons") and April 14, 2015 (indexed at 2015 BCSC 561; the "second Reasons").

[3] Odenza was a construction company involved primarily in building new single-family homes and in undertaking residential renovations. It made an assignment into bankruptcy on December 16, 2013, with serious financial consequences to the owners of unfinished building projects and the suppliers and subcontractors on those projects. The trustee in bankruptcy seized Odenza's operating bank accounts, containing the initial cash balance, which totalled $527,506.22.

[4] The unpaid suppliers and subcontractors were, of course, not only creditors, but, pursuant to section 10 of the *Builders' Lien Act*, SBC 1997, c 45 (the "*BLA*"), also had trust claims against any receivables, and were entitled to register liens against the various job sites to which they provided labour and materials. The total trust and lien claims across all projects approach $3,000,000.

[5] The *Bankruptcy and Insolvency Act*, RSC 1985, c B-3 (the "*BIA*") provides a single forum to deal with the unsecured claims of Odenza's creditors. There is, however, no similar process available for dealing with the trust and lien claims that arose in respect of Odenza's projects, resulting in a number of potential problems: the projects would be tied up in disputes and lien actions, preventing their efficient completion; costs, inconsistencies and inefficiencies would likely result from creditors dealing with trust claims, lien claims and unsecured claims in different forums; and collecting accounts receivable would be more difficult in circumstances where liens were filed against the properties.

[6] In this situation, the trustee proposed a single procedure for the assessment, processing, adjudication and payment out of all claims against Odenza. To accomplish this, the trustee sought an order appointing it as claims administrator to

deal with trust and lien claims in a claims process, called the Trust Claims Settlement Program, or "TCSP", to be undertaken in conjunction with, and complementary to, the claims process under the *BIA*. The trustee would thereafter act in two capacities: as trustee of the bankrupt estate under the *BIA*, and as claims administrator administering the TCSP under the *BLA.* I will refer to him henceforth as the "claims administrator".

[7] I pronounced that order on December 19, 2013, and modified it by order pronounced February 18, 2013. That such modifications proved necessary is not surprising, given that this entire process is relatively novel in both concept and execution. As matters progressed, further complications have arisen.

[8] On June 20, 2014, the claims administrator applied for directions in relation to the distribution of funds, particularly the initial cash balance. Counsel appeared for the claims administrator, and for the trustee. The only other interested party that attended was one of the homeowners, "M". M had made a significant payment to Odenza on November 27, 2013, shortly before the bankruptcy. That payment was made pursuant to the terms of M's contract with Odenza, and was in excess to the amount then owing to subcontractors and suppliers on that project. M took the position that the payment was, or may have been, impressed with a trust in M's favour.

[9] In the first Reasons, I found that the payments made under the contract were not impressed with any such constructive trust, but, depending on the evidence, could consist in part of money that would not fall into a pool of trust funds to be distributed *pro rata* among all lien claimants. I ordered the hearing adjourned for further evidence.

[10] The matter returned before me on March 18, 2015, but the evidence I sought was not yet available. In the second Reasons, I ruled that a statutory trust arising under the *BLA* was capable of meeting the common law requirements for a trust, and thus being exempt from inclusion in the property of the bankrupt under section 67(1) of the *BIA*. I noted that, of the three certainties required by common

law, certainty of intention and certainty of object appeared to be sufficiently established. The problem was whether there was certainty of subject matter. The evidence did not allow me to determine that.

[11] Now, after a third hearing, I find myself in a position to provide the claims administrator with the directions he seeks.

[12] There are lien claimants and unsecured creditors. Some, at least, of the lien claimants would benefit from any trust arising under the *BLA*. That trust, if established on common-law principles, would remove the relevant funds from the estate of the bankrupt and, it follows, from any access by the unsecured creditors. The lien claims far exceed the initial cash balance. The question is whether all or any part of that money impressed by a *BLA* trust, and if so, how it should be distributed.

[13] The parties now agree that, as I suggested in my earlier Reasons, section 10(1) of the *BLA* mandates a "silo" approach. The trust it creates is in relation to funds paid under a contract on a specific project, for the benefit of subcontractors and suppliers to that project. There is no trust in favour of subcontractors and suppliers to other projects of the contractor, nor does the trust extend to payments in excess of lienable expenses on the relevant project through to its completion.

[14] The question I raised in my second Reasons (2015 BCSC 561 at paras 27-30) was whether, in investigating the status of the initial cash balance in the context of the common law requirements for a trust, this "silo" approach had to be maintained. As the claims administrator points out, any such attempt at segregation is complicated by the fact that Odenza breached the trust provisions of the *BLA* by using money collected on particular projects to pay expenses owing on other projects. Hence the bankruptcy.

[15] While the *BLA* provides in section 11(7) that the commingling of funds is not, of itself, a breach of trust, there can be no doubt that the use of funds received on

one project to pay expenses incurred on another *is* a breach, directly contravening section 10(2). The question is whether this affects the analysis of the extent of any trusts arising under the *BLA*. In my view, it does.

[16] The first step is to determine what it is that the initial cash balance comprises. Where did that money come from? In relation to what was it paid? If this cannot be determined with precision, does any purported trust fail for lack of certainty of subject matter? In that event the entire fund will fall into the bankrupt estate for distribution to the unsecured creditors.

[17] Because the monies paid in respect of the various projects were commingled, Odenza's account books offer little assistance. What is clear is that money was paid out very quickly after it came in.

[18] M argues that I should look at the amount paid in on each project, and the lienable expenses claimable against each project, thus following the "silo" approach mandated by section 10 of the *BLA*. It is indeed possible to determine how much was paid in on a particular project, and what expenses were incurred in relation to that project. But that does not deal with what expenses remained to be incurred, and would be claimable against that owner's fund, nor does it deal with the fact that expenses on any given owner's property were in part likely covered by funds paid in by other owners; in any event there is nothing to relate such amounts directly to the initial cash balance.

[19] The claims administrator submits that, from an accounting perspective, the only logical way to examine the cash remaining at the date of bankruptcy is "first in, first out" (FIFO). On this basis, the initial cash balance comprises monies paid in by particular clients of Odenza between December 3 and 13, 2013 that equal or exceed the amount of the initial cash balance. Cash deposits that occurred earlier are assumed to have been dispersed on an FIFO basis, and then replenished by future deposits. Thus, to put it another way, "last paid, still there". Applying this approach, the monies can be identified both as to source and amount. It then becomes possible to assess the trust claims on the funds, to which of the *BLA* trust would

apply, and the surplus of payments in excess of applicable trust claims, which would fall to the bankrupt estate. All monies paid in before this, on this analysis, were spent before the bankruptcy, and are long gone; they are available to no one for anything. Logically, it would follow that any applicable trusts disappeared along with them, even if the monies were paid in breach of those trusts. The trust balance could be distributed only among the lien claimants for the last projects to be funded.

[20] But trusts do not evaporate because the trust property disappears. It is here, then, that the breaches of trust come to the fore. As noted in my second Reasons, there can be no doubt that all of the monies paid by the owners of the various projects at issue were funds that, prior to the bankruptcy, were impressed with trusts by section 10(1) of the *BLA*. Those trusts remained until the beneficiaries were paid. The problem is that any attempt after the bankruptcy to assess what remains in trust on a project-by-project basis is frustrated by Odenza's breaches (paying sub trade claims of one job with funds received from other jobs). On a FIFO approach, the effect would be to limit the trusts to the last few standing – last in, still there.

[21] But the law is quite clear that FIFO is the wrong approach to the distribution of mingled trust funds where the trust claims exceed the amount available. The correct approach is to distribute the funds pro rata: *Law Society of Upper Canada v Toronto Dominion Bank* (1998), 42 OR (3d) 257 (CA) and *Re Ontario Securities Commission and Greymac Credit Corp.* (1986), 59 OR (2d) 480 (CA), upheld [1988] 2 SCR 172.

[22] The law also provides that where a trustee acts in breach of trust in the mingling and spending of trust and non-trust funds, he is deemed to have spent his own money first, and trust money last: *Re Hallett's Estate*: *Knatchbull v Hallett* (1880) 13 Ch D 696 (CA).

[23] This case is quite a different from the situation considered in *Royal Bank of Canada v Atlas Block Co*, 2014 ONSC 3062, where only part of the bankrupt's business could be subject to liens under the *Construction Lien Act*, RSO 1990, c C-30. Here, all of the funds paid to Odenza were subject to the *BLA*. Given the certainty of the subject matter of the trusts when the funds were received by the

Odenza, can the trusts be vitiated by uncertainty caused by the trustee's breaches in handling the funds and in distinguishing between trust funds and non-trust funds? In my view, it cannot.

[24] I conclude, in all of the circumstances of this unusual case, that the entire initial cash balance must be considered to comprise funds held in trust pursuant to the provisions of the *BLA*, which are to be distributed *pro rata* to all trust and lien claimants. Nothing remains for the trustee of the bankrupt estate.

[25] I appreciate that this is of little comfort to owners such as M who paid funds in excess of existing lienable claims but will get nothing, and remain potentially liable for amounts they did not hold back in accordance with the requirements of the *BLA*. Regrettably there is no way through this to a good outcome.

[26] The remaining matters are not controversial. The order will go in the form attached as Schedule "A" to the Amended Notice of Application, subject to any necessary changes flowing from these Reasons. If there is any difficulty, the parties are at liberty to apply.

"GRAUER, J."